

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
AGL WELDING SUPPLY CO., INC.	:	DETERMINATION
	:	DTA NO. 807194
for Revision of a Determination or for Refund	:	
of Sales and Use Taxes under Articles 28 and 29	:	
of the Tax Law for the Period September 1, 1984	:	
through May 31, 1987.	:	

Petitioner, AGL Welding Supply Co., Inc., 600 Route 46 West, Clifton, New Jersey 07150, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1984 through May 31, 1987.

A hearing was held before Dennis M. Galliher, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on September 21, 1992 at 1:15 P.M., with all briefs to be submitted by January 11, 1993. Petitioner, appearing by Orbe, Nugent, Collins & Darcy, Esqs. (John F. Darcy, Esq., of counsel), submitted a brief on November 30, 1992. The Division of Taxation, appearing by William F. Collins, Esq. (James Della Porta, Esq., of counsel), submitted a responding brief on December 30, 1992. Petitioner submitted its reply brief on January 11, 1993.

ISSUES

I. Whether petitioner's purchases of industrial gas cylinders were purchases for resale within the meaning of Tax Law § 1101(b)(4) not subject to the imposition of sales tax.

II. Whether, if such purchases were not for resale, the Division of Taxation is nonetheless estopped from asserting such tax based on its prior determination not to impose tax against petitioner.

III. Whether, assuming tax is due, petitioner has established sufficient basis to warrant reduction or abatement of penalties.

FINDINGS OF FACT

Petitioner, AGL Welding Supply Co., Inc. ("AGL"), is engaged in the business of selling industrial and medical gases, as well as hard goods for welding such as rods, wire, cable and welding machines. Petitioner also sells medical breathing assistance devices. The industrial and medical gases sold by petitioner are delivered in compressed gas cylinders which have substantial steel walls allowing the gas to be contained under pressure. As more fully detailed hereinafter, petitioner sells gas to various customers in those customers' own cylinders, and also sells gas contained in cylinders owned (or rented) by petitioner.

On May 2, 1989, the Division of Taxation ("Division") issued to petitioner two notices of determination and demands for payment of sales and use taxes due. The first of such notices assessed sales tax due for the period September 1, 1984 through May 31, 1987 in the amount of \$47,187.00, plus penalty and interest. The second such notice assessed omnibus penalty (only) in the amount of \$2,934.50 for the period September 1, 1985 through February 28, 1987. Petitioner had previously executed a series of consents extending the period of limitations on assessment whereby assessment for the period September 1, 1984 through February 28, 1986 could be made at any time on or before June 20, 1989.

Neither the audit methodology employed by the Division nor the mathematical accuracy of the resulting dollar amount of tax as calculated are contested. In fact, petitioner has conceded and paid \$2,385.00 against the above assessment, relating to certain nontaxable sales disallowed upon audit. Therefore, remaining at issue herein is the sum of \$44,802.00 assessed on petitioner's purchases (or rentals) of gas cylinders, plus related penalties and interest.

As described, petitioner sells industrial and medical gases to customers who do not lease cylinders from petitioner. Petitioner also leases empty cylinders to one customer (IBM) who does not purchase its gas from petitioner. This latter transaction involves the leasing of approximately 735 cylinders. However, most of petitioner's customers obtain from petitioner industrial or medical gases contained in cylinders owned (or rented) by petitioner.

Petitioner invoices its customers separately for gas purchases and for cylinder rentals. Petitioner ships or delivers filled cylinders to its customers and takes back empty cylinders in

return. Petitioner's customers are billed on the 25th day of each month for all cylinders then in their possession. The charge for each cylinder depends on the type of cylinder involved. A customer who purchased no gas in the rental period would nonetheless be charged a rental fee for all cylinders in its possession on the 25th day of the month. As described in testimony a customer could, in theory, avoid a rental charge by returning all cylinders in its possession before the 25th day of the month. However, in contrast, a party who took an initial delivery of cylinders on the 24th day of the month would be billed for a full month's possession of those cylinders on the 25th day of the month (i.e., the next day). It would appear that, in practice, those customers who purchased gas contained in petitioner's cylinders did so on an ongoing "rollover" or "running count" basis, as evidenced by petitioner's accounting/invoicing system for cylinders (i.e., cylinders delivered beginning balance, plus cylinders delivered during the month, minus cylinders returned, equals ending balance of cylinders [as of the 25th of each month]).

Petitioner had total sales of \$13,492,223.85 for the year 1986, out of which gas sales totalled \$5,096,929.88, and cylinder rental fees totalled \$1,963,436.76. From these figures, petitioner calculates cylinder rental fees as 14.5% of total sales, and 38.5% of the amount of gas sales.

Petitioner collected from its customers and paid to the Division sales tax on all of its rental charges for cylinders (except where such rentals were otherwise exempt, e.g., to tax-exempt organizations). It did not, however, pay sales tax on its own purchases (or rentals) of such cylinders, as it considered the same to be purchases for resale (by rental).

The reverse side of each of petitioner's cylinder rental invoices, at paragraphs "5", "6" and "7", contains the following language:¹

- "5. Buyer agrees that gas cylinders remain the property of Seller and are loaned on rental and not sold; that gas cylinders appreciate rather than depreciate in value through age or usage. Buyer therefore agrees to pay Seller at Seller's

¹The quoted language appears in the record in a rider attached to the petition (and is also repeated in petitioner's brief). While actual invoices carrying such language were not offered in evidence, there does not appear to be any dispute that such language in fact appears on petitioner's cylinder rental invoices.

- then current price, as shown in Seller's monthly cylinder rental invoice and monthly cylinder master file book, for any loss, destruction, or damage beyond repair of any cylinder, fitting or equipment resulting from any cause after delivery to the Buyer. In case of damage permitting repairs, Buyer agrees to pay the actual cost of repair incurred by Seller plus cost of transportation and any other charges. Failure to return any cylinder after ninety (90) days shall be deemed to be a loss within the meaning of paragraph 5. No claim that cylinders have been returned by Buyer will be valid unless Buyer holds a valid signed receipt on the form provided by Seller evidencing such return. The refilling of cylinders by another supplier without Seller's written consent is prohibited, a violation of law, and a breach of this agreement.
- "6. It is agreed that, until all cylinders loaned by the Seller to the Buyer are returned to Seller, any loss or damage except ordinary wear and tear to such cylinders or to any part or accessory thereof, are assumed by Buyer even though such loss or damage is attributable to an act of God or other catastrophic occurrence. The quantity of cylinders and applicable rental charges set forth on Seller's monthly rental statement shall be conclusively presumed to be correct unless, with respect to any such monthly statement, Buyer shall notify Seller in writing, within thirty (30) days of receipt thereof, that Buyer disputes the correctness thereof and sets forth in such notice, in reasonable detail, the facts upon which dispute is based. Until such cylinders are returned or until the cylinders are paid for if lost, Buyer shall be responsible for payment of rent on the cylinders and compounded Finance Charges on any unpaid rental charges, charges for lost cylinders, charges for product, and unpaid Finance Charges.
- "7. Payment of Cylinder Rental invoices acknowledges that the total cylinders shown in Buyer's possession on the date shown is correct. Buyer therefore agrees that if legal proceedings are instituted [sic] to collect charges for lost cylinders, proof of cylinders shipped and returned need only commence with the last Cylinder Rental Invoice which was paid in full."

Petitioner noted that the one customer who rented empty cylinders on a monthly basis (IBM) was charged the same cylinder rental fees as were petitioner's other customers. Petitioner also noted that approximately 5% of its gas sales were not sales of gas contained in petitioner's cylinders (i.e., a customer would bring in its own cylinders for fill-up). In these instances, petitioner charged the same price for the gas as was charged for gas delivered in petitioner's cylinders.

During the year immediately preceding the start of the period in question here, the Division had assessed sales tax liability against petitioner with respect to cylinders petitioner was acquiring as part of its bulk sale acquisition of another entity. Petitioner notes, and placed in the record evidence to support, the Division's withdrawal of such assessment upon the

conclusion that petitioner was purchasing such cylinders for resale via re-rental. In turn, petitioner maintains that the Division must be "judicially estopped" from changing its position and assessing tax as it has herein. Petitioner also maintains, in any event (assuming tax is due and estoppel does not apply), that penalties are inappropriate and must be abated given the Division's change of position.

CONCLUSIONS OF LAW

A. A retail sale is defined by the Tax Law to include a sale of tangible personal property to any person for any purpose other than for resale (Tax Law § 1101[b][4][i]). All such retail sales are subject to tax unless excluded or exempted therefrom by a specific provision of the Tax Law (Tax Law § 1105[a]).

B. As used in the Tax Law, the term sale is defined as:

"Any transfer of title or possession or both, exchange or barter, rental, lease or license to use or consume, conditional or otherwise, in any manner by any means whatsoever for a consideration" (Tax Law § 1101[b][5]).

20 NYCRR 526.7(e)(4) provides that with respect to a "rental", transfer of possession has occurred where there has been a transfer of "custody or possession of the tangible personal property, actual or constructive" (20 NYCRR 526.7[e][4][i]).

C. Petitioner argues that all of the cylinders it purchased were purchased for subsequent rental, and in fact were rented, thus maintaining that its cylinder purchases were not properly subject to sales tax under Tax Law § 1101. As a general principle, tangible personal property which a vendor incidentally supplies to its customers as a part of the vendor's rendering of a taxable service is not deemed to be purchased for resale. On this basis it has been found that, absent a separate charge, trash containers provided by a waste hauler to its customers were not purchased by the hauler for resale (Matter of U-Need-A-Roll Off Corp. v. New York State Tax Commn., 67 NY2d 690, 499 NYS2d 921; see also, Matter of Laux Advertising v. Tully, 67 AD2d 1066, 414 NYS2d 53). In Matter of Albany Calcium Light Co. v. State Tax Commn. (44 NY2d 986, 408 NYS2d 333), the Court of Appeals held that the purchase for resale exclusion did not apply to purchases of gas cylinders by a vendor which did not ordinarily impose a

separate charge for its customers' use of the cylinders, but did impose a demurrage charge if the cylinders were kept beyond 30 days. The court found that the demurrage charge did not mean that the cylinders were purchased for the purpose of renting them to customers since the vendor "did not acquire the cylinders with the expectation of collecting these unusual charges which are purely incidental to its primary business of selling gas" (Matter of Albany Calcium Light Co., supra at 988).

D. In all of the above-cited cases, the vendor imposed no charge for the property transferred to its customer (except in unusual circumstances) and provided such property only as an incident to its primary business (i.e., the vendor was not in the business of renting or selling tangible personal property to its customers). Accordingly, there are two factors which must be looked at to determine whether a vendor's purchase of tangible personal property is for the purpose of subsequent resale or rental: (1) whether the vendor separately bills its customers for use of the tangible personal property; and (2) whether rental of the property is a component of the vendor's business rather than a mere incident to the vendor's primary business (cf., Matter of Atlas Linen Supply Co., State Tax Commission, August 27, 1987). If these two factors indicate a purchase for resale or rental, the vendor must also show that the tangible personal property is purchased exclusively for resale and is not also used for other purposes (Matter of Micheli Contr. Corp. v. New York State Tax Commn., 109 AD2d 957, 958, 486 NYS2d 448).

E. In Matter of Valley Welding Supply Co. v. Chu (131 AD2d 917, 516 NYS2d 366) the three factors discussed above were examined. There, the vendor presented its customers with three payment alternatives for the use of its cylinders: (1) the cylinder could be rented on a per diem basis; (2) the cylinder could be leased under a traditional lease arrangement for a period of a year or more; or (3) no initial charge would be imposed for use of the cylinder for the balance of the calendar month in which delivery was made but, thereafter, a monthly use charge was imposed. The latter charge, also referred to as a demurrage, accounted for at least 50 percent of all cylinder use charges petitioner imposed.

The vendor's invoices separately stated a charge for the cylinder's use under one of the

three plans and a charge for the gas consumed. At the administrative hearing, the Division conceded that the first two payment alternatives were rental arrangements which, standing alone, would qualify for the resale exemption; however, it argued that the cylinders used in the demurrage plan were not purchased exclusively for resale because the possibility existed that customers would return the cylinders during the grace period without paying any rental fee for their use. The State Tax Commission concluded that under the demurrage plan cylinders not retained for more than 30 days were not rented and thus some cylinders were used for purposes other than rental; since all of the cylinders were used interchangeably, in all three payment plans, none of the cylinders was purchased exclusively for resale and, hence, all were subject to sales tax when purchased by the vendor (Matter of Valley Welding Supply Co., State Tax Commission, November 7, 1985, confirmed 131 AD2d 917, 516 NYS2d 366).

F. The Division maintains that petitioner's month-to-month leasing arrangement is analogous to the demurrage plan in Valley Welding. In Valley Welding, each cylinder placed in the customer's possession was identified through billing records and no charge was made if the cylinder was returned within 30 days; as a consequence, a high volume gas user would never pay a cylinder rental, since it would repeatedly return empty cylinders for filled ones within 30 days. By contrast, petitioner's invoices do not identify each cylinder individually (e.g., by serial numbers), but rather list the total number of each type of cylinder delivered and returned. Petitioner contrasts the Valley Welding situation with its own plan where a cylinder user would not avoid a rental charge through frequent turnover because it would be charged a monthly fee for all cylinders in its possession on the 25th day (and would only avoid a charge if it had no cylinders in its possession on the 25th). An example drawn from petitioner's method of billing demonstrates the difference between its month-to-month plan and the demurrage plan of Valley Welding. A customer with a beginning monthly inventory of 20 cylinders, which returned 20 empty cylinders and took delivery of 20 filled cylinders during the month, would have 20 cylinders in its inventory on the 25th day of the month. This customer would pay a rental charge on 20 cylinders under petitioner's plan but would have paid no rental charge under the

Valley Welding demurrage plan. Petitioner argues that its month-to-month plan is a traditional leasing arrangement rather than a demurrage plan. The Division notes that a customer has the option of returning all cylinders to petitioner before the 25th day of the month, thus avoiding the rental charge altogether; however, there is no evidence to show that such an event has occurred or that the same would be anything but highly unusual. The possibility of its occurring is not sufficient to establish that petitioner's month-to-month leasing plan here is identical to the demurrage plan in Valley Welding.

G. To determine whether petitioner's purchases of gas cylinders qualified for the resale exclusion, it is necessary to apply the three factors outlined above to petitioner's actual business practices and leasing arrangements. First, it is clear that petitioner separately states a charge on each invoice for the sale of gas and the rental of the cylinder in which the gas is delivered. Second, petitioner rents unfilled cylinders (see Finding of Fact "4") and certainly derives a substantial amount of revenue from its overall cylinder rental charges (see Finding of Fact "6"). Accordingly, the rental of gas cylinders was a component of petitioner's overall business and was not merely incidental to its sale of industrial and medical gases. In addition, it is undisputed that petitioner collected and paid over sales tax with regard to such rental receipts (see Finding of Fact "7"). The third factor, whether petitioner purchased its cylinders exclusively for rental, presents a more difficult question. Gas, under pressure, must be housed in a suitable container at all times. Petitioner sold gas to customers who provided their own containers, but these transactions were not the lion's share of petitioner's business (see Finding of Fact "9"). For the most part, petitioner delivered gas to its customers in its own cylinders. To the extent that a rental cannot be said to have occurred until actual possession of the cylinder was transferred to the customer (cf., Matter of Waste Mgt. v. Tax Appeals Tribunal, 185 AD2d 479, 585 NYS2d 883, lv denied 80 NY2d 762, 592 NYS2d 670; Matter of Shanty Hollow Corp v. New York State Tax Commn., 111 AD2d 968, 969, 490 NYS2d 67), some element of self-use was always present in the cylinder transactions. However, petitioner intended to and did, as evidenced by its practices, collect a rental charge each time one of its cylinders was delivered to

and used by a customer, and there is no evidence to show that cylinders were not rented (i.e., were made available and/or accounted for in a manner other than as described herein). The possibility that a customer could return all cylinders before the 25th of the month and avoid a rental charge is insufficient basis to conclude that petitioner's cylinder rental practice was the same as the demurrage plan in Valley Welding. Hence, petitioner purchased the cylinders for resale within the meaning of Tax Law § 1101(b)(4)(i) and (5). This conclusion is consistent with the Division's position in Valley Welding, where it conceded that the purchase of cylinders subsequently rented under the terms of a traditional lease arrangement would qualify for the resale exclusion, although they were rented in connection with the sale of gas.

H. In light of the foregoing, Issues II and III are rendered moot.

I. The petition of AGL Welding Supply Co., Inc. is granted, and the notices of determination and demands for payment of sales and use taxes due dated May 2, 1989 are cancelled.

DATED: Troy, New York
July 1, 1993

/s/ Dennis M. Galliher
ADMINISTRATIVE LAW JUDGE